

Message Text

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C O N F I D E N T I A L SECTION 01 OF 03 BONN 01903

LIMDIS

PASS TREASURY FOR ASSISTANT SECRETARY COOPER & L.WIDMAN
OECD PARIS FOR KORP

E.O. 11652: GDS

TAGS: EFIN, GW

SUBJECT: GERMAN POSITION ON THE SOLIDARITY FUND

1. SUMMARY: WE HAVE SET OUT BELOW WITH OUR COMMENTS THE POSITION OF OUR FINANCE MINISTRY CONTACTS ON LEGAL, TECHNICAL AND POLITICAL ASPECTS OF A GERMAN CONTRIBUTION TO THE SOLIDARITY FUND. THE VIEWS OF STATE SECRETARY POEHL ARE BEING REPORTED SEPARATELY. EVEN THOUGH INTERNAL POLITICAL CONSIDERATIONS ARE THE MAIN REASONS WHY THE FEDERAL REPUBLIC OPPOSES A DIRECT FEDERAL BUDGET CONTRIBUTION TO THE SOLIDARITY FUND, WE HAVE GONE IN SOME DETAIL INTO THE CONSTITUTIONAL ARGUMENTS BECAUSE OF THE EMPHASIS MUELLER-ENDERS, THE GERMAN MEMBER OF THE WORKING GROUP, PUTS ON THEM AND BECAUSE THEY ALSO APPLY TO SOME FORMS OF GUARANTIES AND ARE BEHIND SOME OF THE GERMAN POSITIONS ON THAT QUESTION. END SUMMARY.

2. DIRECT BUDGET CONTRIBUTION: A POLITICAL DECISION HAS BEEN MADE AGAINST COMMITTING THE FEDERAL REPUBLIC
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AT THIS TIME TO THE POSSIBILITY OF A DIRECT CONTRIBUTION

FROM THE FEDERAL REPUBLIC AND THE FINANCE MINISTRY LAWYERS ARE THEREFORE INSISTING THAT AN AGREEMENT CAN ONLY BE SIGNED IF THE COMMITMENT OF THE FEDERAL REPUBLIC TO CONTRIBUTE TO THE SOLIDARITY FUND CAN CLEARLY BE FULFILLED IN SOME OTHER MANNER (I.E., GUARANTIES OR BUNDESBANK CONTRIBUTION). FINANCE MINISTER APEL IS PUBLICLY ON RECORD AGAINST A FEDERAL BUDGET CONTRIBUTION AND IS UNLIKELY TO REVERSE HIMSELF ON THIS POINT. IN ADDITION, THE FINANCE MINISTRY LAWYERS MAINTAIN THAT EVEN IF APEL SO DESIRED, A BUDGET CONTRIBUTION IS NOT POSSIBLE AT THIS TIME BECAUSE OF THE LARGE DEFICIT IN THE CURRENT BUDGET AND ARTICLE 115 OF THE BASIC LAW WHICH LIMITS THE AMOUNT OF FEDERAL BORROWING DURING ANY ONE BUDGET YEAR TO THE MAGNITUDE OF INVESTMENT EXPENDITURES IN THE SAME FEDERAL BUDGET (SEE BONN 1044). MUELLER-ENDERS TELLS US THAT HE HAS PRESSED FOR A LEGAL INTERPRETATION WHICH WOULD BRING BORROWING OF MONEY FOR A CONTRIBUTION TO THE SOLIDARITY FUND UNDER THE EXCEPTIONS TO THE DEBT LIMITATIONS OF ARTICLE 115 FOR BORROWING NECESSARY TO "AVERT A DISTURBANCE OF THE OVERALL ECONOMIC EQUILIBRIUM." THE FINANCE MINISTRY LAWYERS, HOWEVER, HAVE REFUSED TO GO ALONG AND HAVE ARGUED THAT THIS EXCEPTION APPLIES ONLY TO DOMESTIC COUNTERCYCLICAL SPENDING BECAUSE ONLY DOMESTIC SPENDING WAS CONSIDERED DURING THE PARLIAMENTARY DEBATES AT THE TIME ARTICLE 115 WAS ENACTED AND EXTERNAL SPENDING OR DISEQUILIBRIUM WERE NOT EVEN MENTIONED. WE FIND IT DIFFICULT TO CONSIDER THIS ARGUMENT FULLY CONCLUSIVE. IN ADDITION, SINCE FUNDS ARE FUNGIBLE, IT COULD BE ARGUED THAT ANY PORTION OF FEDERAL BORROWING IN EXCESS OF THE LIMITATIONS OF ARTICLE 115 IS FOR DOMESTIC PURPOSES WHILE A GERMAN CONTRIBUTION TO THE SOLIDARITY FUND IS PAID OUT OF REGULAR REVENUES OR BORROWING WITHIN THE LIMITATION OF ARTICLE 115. SUCH AN INTERPRETATION WOULD MAKE POSSIBLE A BUDGET CONTRIBUTION AT LEAST DURING 1975 WHEN THE INTERNAL CYCLICAL SITUATION CALLS FOR DEFICIT SPENDING. FINALLY, ONE COULD ARGUE THAT A GERMAN CONTRIBUTION TO THE SOLIDARITY FUND IS "AN INVESTMENT"

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UNDER ARTICLE 115 AND THUS AUTOMATICALLY INCREASES THE DEBT LIMIT. OTHER FEDERAL LOANS AND CONTRIBUTIONS SUCH AS THE FEDERAL OFFSET LOAN TO THE US IN 1969/71, BILATERAL GERMAN AID FOR CAPITAL PROJECTS, THE GERMAN PARTICIPATION IN IDA AND THE IDB ARE ALL FINANCED THROUGH THE GERMAN FEDERAL BUDGET AND ARE TREATED IN GERMAN BUDGET ACCOUNTING AS "INVESTMENTS." WE RECEIVE THE FOLLOWING ANSWERS IN REBUTTAL WHEN

MENTIONING THESE PRECEDENTS TO GERMAN OFFICIALS.
REGARDING AN EXCEPTION TO ARTICLE 115 FOR INTERNAL
COUNTERCYCLICAL FINANCING, WE ARE TOLD THE FEDERAL

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GOVERNMENT DOES NOT WANT TO ADMIT THAT DEGREE OF
INTERNAL DISEQUILIBRIUM. REGARDING LOANS AS
"INVESTMENT," WE ARE TOLD THAT A DISTINCTION HAS TO
BE MADE BETWEEN LOANS FOR "SPECIFIC CAPITAL PROJECTS"
ABROAD AND CONTRIBUTIONS TO INTERNATIONAL
DEVELOPMENT BANKS, BOTH OF WHICH PROPERLY CAN BE
CONSIDERED AS AN "INVESTMENT" UNDER ARTICLE 115 AND
OTHER FOREIGN AID SUCH AS INTEREST SUBSIDIES, TECHNICAL
AID AND BALANCE OF PAYMENTS AID WHICH CANNOT BE
CONSIDERED AS INVESTMENTS. (COMMENT: THIS IS TRUE
IN PAST GERMAN BUDGET ACCOUNTING FOR SUBSIDIES AND
TECHNICAL AID, WHICH ARE NOT CLASSIFIED AS INVESTMENTS,
BUT WE HAVE NOT YET BEEN ABLE TO LOCATE A PRECEDENT
ONE WAY OR THE OTHER FOR BILATERAL BALANCE OF PAYMENTS
AID UNLESS THE 1969/71 US OFFSET LOAN IS CONSIDERED
AS SUCH AID. THIS OFFSET LOAN WAS TREATED AS AN
INVESTMENT IN BUDGET ACCOUNTING AT THE TIME.) WHEN
RAISING THE 1969 OFFSET LOAN, WE ARE TOLD THAT THE

FEDERATION NOW IS FOR THE FIRST TIME APPROACHING THE DEBT LIMITATION UNDER ARTICLE 115 AND THAT PAST BUDGET ACCOUNTING (SUCH AS THAT FOR THE US OFFSET LOAN) IS NOT NECESSARILY DETERMINING NOW THAT THE ISSUE OF WHETHER OR NOT AN ITEM IS AN INVESTMENT IS FOR THE CONFIDENTIAL

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FIRST TIME OF ACTUAL CONSEQUENCE AND CONSTITUTIONAL RELEVANCE.

3. AS INDICATED ABOVE, WE BELIEVE A CASE COULD BE MADE THAT A DIRECT FEDERAL BUDGET CONTRIBUTION TO THE SOLIDARITY FUND WOULD NOT VIOLATE THE DEBT LIMITATION OF ARTICLE 115 OF THE GERMAN BASIC LAW (CONSTITUTION). BUT IN VIEW OF THE VIRGIN TERRITORY COVERED BY THE INTERPRETATION OF ARTICLE 115, THE FINAL RULING OF THE CONSTITUTIONAL COURT ON THESE QUESTIONS REMAINS VERY UNCERTAIN. IN VIEW OF THIS AND THE FACT THAT THE GERMAN GOVERNMENT IN ANY CASE DOES NOT FAVOR A DIRECT BUDGET CONTRIBUTION, IT IS NOT SURPRISING THAT THE FINANCE MINISTRY LAWYERS AND CIVIL SERVANTS ARE CONCENTRATING ON FINDING WAYS OF IMPLEMENTING THE GERMAN COMMITMENT TO THE SOLIDARITY FUND WHICH AVOID THE CONSTITUTIONAL DEBT LIMITATION ISSUE RATHER THAN ON FINDING WAYS OF MEETING THAT ISSUE. THE FINANCE MINISTRY IS PARTICULARLY GUN-SHY OF CONSTITUTIONAL ISSUES AT THIS TIME BECAUSE OF THE READINESS OF THE OPPOSITION PARTY TO BRING SUIT IN THE CONSTITUTIONAL COURT (FOR EXAMPLE, ON SCHMIDT'S YEAR-END SPENDING IN 1973) AND THE GENERAL HEATING UP OF THE POLITICAL CLIMATE AS SOME KEY STATE ELECTIONS ARE APPROACHING THIS SPRING.

4. GUARANTIES: CONSTITUTIONAL DEBT LIMITATION PROBLEMS SPILL OVER INTO THE GERMAN POSITION ON GUARANTIES BECAUSE THE FINANCE MINISTRY LAWYERS TAKE THE POSITION THAT A FEDERALLY GUARANTEED LOAN RAISED BY A GERMAN INSTITUTION FOR THE PURPOSE OF FINANCING THE GERMAN CONTRIBUTION TO THE SOLIDARITY FUND WOULD BE A SO THINLY VEILED CIRCUMVENTION OF ARTICLE 115 THAT SUCH A LOAN, TOO, WOULD FALL UNDER THE DEBT LIMITATION OF THAT ARTICLE AND IN ADDITION MIGHT BE CONSIDERED BY THE PARLIAMENT AS A CIRCUMVENTION OF THE PROPER BUDGETARY PROCESSES. MUELLER-ENDERS GOES SO FAR AS TO SAY THAT SUCH A GUARANTY SUBSEQUENTLY MIGHT BE DECLARED UNCONSTITUTIONAL AND VOID BY THE COURTS AND THAT THIS POSSIBILITY MIGHT AFFECT THE MARKETABILITY OF SUCH A LOAN ISSUE. THE MINISTRY CONFIDENTIAL

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EXPERTS BELIEVE, HOWEVER, THAT THEY CAN AVOID THIS PROBLEM IF INSTEAD THE GUARANTY IS EXTENDED TO A LOAN BY AN INTERNATIONAL INSTITUTION WHICH ITSELF IS PART OF THE RECYCLING PROCESS.

5. BUNDESBANK: THE DIFFICULTIES OF HAVING THE BUNDESBANK INVEST SOME OF ITS FOREIGN EXCHANGE RESERVES IN THE SOLIDARITY FUND ARE NOT OF A CONSTITUTIONAL OR LEGAL NATURE. IN HOW TO USE ITS RESERVES, THE BUNDESBANK IS LARGELY ITS OWN JUDGE OF WHAT IS PROPER. GENERALLY SUCH INVESTMENTS HAVE TO BE LIQUID AND SHORT TERM. BUT WITH THE AGREEMENT OF THE CENTRAL BANK COUNCIL THESE CONCEPTS CAN BE STRETCHED CONSIDERABLY. A VARIETY OF TECHNIQUES HAVE BEEN USED IN THE PAST. THUS, FOR EXAMPLE, THE BUNDESBANK IS COMMITTED TO MAKE GERMAN CONTRIBUTIONS TO THE IMF GENERAL AGREEMENT TO BORROW WHICH TAKE THE FORM OF LOANS OF AS LONG AS 5 YEARS MATURITY, BUT WHICH CONTAIN A REVERSIBILITY CLAUSE REQUIRING THE IMF TO REPAY THEM PREMATURELY IF THE CREDITOR'S BALANCE OF PAYMENTS

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POSITION DETERIORATES. SIMILARLY THE BUNDESBANK HAS EXTENDED 7-YEAR LOANS TO THE US UNDER THE LAST OFFSET AGREEMENT. THE MOBILIZATION CLAUSE IN THIS CASE PROVIDES THAT THE SECURITIES CAN BE CASHED PREMATURELY AT PAR IF THE BUNDESBANK'S LIQUID FOREIGN EXCHANGE RESERVES SHOULD DECLINE TO A POINT WHICH WOULD OTHERWISE REQUIRE THE USE OF CREDIT ARRANGEMENTS. A DIFFERENT TECHNIQUE WAS USED IN CASE OF THE GERMAN \$2 BILLION GOLD LOAN TO ITALY. THIS TOO IS PROVIDED BY THE BUNDESBANK. THE LIQUIDITY OF THE BUNDESBANK'S INVESTMENT IS FORMALLY ASSURED SINCE IT TAKES THE FORM OF 6-MONTH RENEWABLE CREDITS AND IS BACKED BY ITALIAN GOLD.

6. ALL OF OUR GOVERNMENT CONTACTS, HOWEVER, BELIEVE THAT IT IS VERY DOUBTFUL IF A CENTRAL BANK COUNCIL AGREEMENT COULD BE OBTAINED AT THIS TIME TO A BUNDESBANK ASSUMPTION OF THE GERMAN OBLIGATION TO THE SOLIDARITY FUND. THE GOVERNMENT PREFERS NOT TO APPROACH THE BUNDESBANK IN THIS REGARD NOW (OTHER THAN ON ARRANGEMENTS FOR SWAP PREFINANCING OF SOLIDARITY FUND ASSISTANCE). IT DOES NOT EXCLUDE THE POSSIBILITY, HOWEVER, OF BUNDESBANK PARTICIPATION ONCE CONCRETE CASES ARISE.

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